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Digital Music Garage Sale: An Analysis of Capitol Records, LLC v. ReDigi Inc. and a Proposal for Legislative Reform in Copyright Enabling a Secondary Market for Digital Music

Nicholas Costanza

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Digital Music Garage Sale: An Analysis of *Capitol Records, LLC v. ReDigi Inc.* and a Proposal for Legislative Reform in Copyright Enabling a Secondary Market for Digital Music

by NICHOLAS COSTANZA*

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Digital music has become the ubiquitous soundtrack of American life.

– Rick Carnes, President of Songwriters Guild of America

I. Introduction

For as long as vinyl records, cassette tapes, and CDs have been platforms for storing and distributing music, copyright law has provided consumers a right to resell their lawfully purchased music on these platforms without permission from the copyright holder.¹ While these

* J.D. Candidate, University of California Hastings College of the Law 2015; B.A., California State Polytechnic University, Pomona 2012; Executive Editor, *Hastings Communications and Entertainment Law Journal*. I would like to thank my parents, Dennis and Jane, for their continued support and encouragement. I would also like to thank Kevin Kearney and the Comm/Ent production staff for their editorial contributions to this note.

physical platforms are still made available to consumers today, rapid technological advances have caused a swift and—at least according to some—problematic transition from physical to digital platforms. In fact, The Nielsen Company and Billboard's 2012 Music Industry Report touted that music purchases—fueled by an increase in digital sales, despite a decrease in physical sales—were actually at an all-time high.²

While digital music has revolutionized the way music is heard, shared, and purchased over the Internet, several side effects—the most prevalent being illegal downloading and peer-to-peer file sharing—have changed the economics of the music industry.³ Initially, artists, record companies, and organizations in the interest of copyright holders were resistant to embracing digital music platforms and viewed them as a threat to the rights of artists and copyright holders.⁴ Despite an initial decline in physical sales resulting from digital media technology, copyright holders have developed methods for generating revenue through digital sales⁵ and streaming royalties.⁶ In fact, the music industry has a history of claiming new technologies will “kill” the current business model, while simultaneously profiting from the exact technology it criticizes.⁷ Thus, the most significant issues resulting from the clash of digital media technology and copyright law have primarily involved the interests of copyright holders. In recent years, however, at least some of that focus shifted to how digital media technology affects the interests of consumers and what they may do with the music they purchase.

1. See 17 U.S.C. § 109(a) (2013) (“[T]he owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.”); see generally *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908) (holding that the owner of a copyrighted work may subsequently sell that copyrighted work without violating the copyright holder's right to distribution).

2. *The Nielsen Company & Billboard's 2012 Music Industry Report*, BUSINESS WIRE, Jan. 4, 2013, <http://www.businesswire.com/news/home/20130104005149/en/Nielsen-Company-Billboard%E2%80%99s-2012-Music-Industry-Report#.UySG8UJdWvI>.

3. See *Peer-to-Peer File Sharing: A Guide for Business*, BUREAU OF CONSUMER PROT., available at <http://www.business.ftc.gov/documents/bus46-peer-peer-file-sharing-guide-business#Whatis> (last visited Mar. 1, 2014) (defining peer-to-peer file sharing as “a way to share music [that] enables computers using the same or compatible P2P programs to form a network and share digital files directly with other computers on the network”).

4. Eric Pfanner, *Music Industry Sales Rise, and Digital Revenue Gets the Credit*, N.Y. TIMES, Feb. 26, 2013, available at http://www.nytimes.com/2013/02/27/technology/music-industry-records-first-revenue-increase-since-1999.html?_r=0.

5. See, e.g., *Content Providers: Frequently Asked Questions*, APPLE, <http://www.apple.com/es/itunes/contentproviders/faq.html> (last visited Mar. 10, 2014).

6. Kristin Thompson, *Music and How the Money Flows*, FUTURE OF MUSIC COAL., June 18, 2013, <http://futureofmusic.org/article/article/music-and-how-money-flows>.

7. See generally Mark A. Lemley, *Is the Sky Falling on the Content Industries?*, 9 J. ON TELECOMM. & HIGH TECH. L. 125 (2011).

In 2011,⁸ a Massachusetts-based tech company called ReDigi, Inc. sparked a strong debate about digital music consumers' rights by creating the first resale marketplace for lawfully purchased digital music.⁹ Technological advancements in digital music are typically faced with fierce and immediate challenges from copyright holders. Moreover, the creation of a secondary digital marketplace by ReDigi's CEO, John Ossenheimer,¹⁰ proved to be no different in light of Capitol Records, LLC's (Capitol) copyright infringement claim against ReDigi just three months after the site launched.¹¹

Despite ReDigi's efforts to comply with copyright law¹² and to distinguish itself from infringing services (such as Napster¹³ and Bopaboo¹⁴), the United States District Court for the Southern District of New York ultimately held that ReDigi's services violated Capitol's exclusive rights under the Copyright Act of 1976 (the "Act").¹⁵ The court's insistence on avoiding issues of policy and technology—opting instead to focus on the text of the Act—illustrates a time in which copyright law, and the technology required to operate within the confines of that law, may no longer coexist absent legislative change.¹⁶

This note explains the *ReDigi* case and discusses the complex relationship between "secondary digital market" technology and current copyright law—specifically, copyright holders' exclusive right to reproduction and content owners' "first sale" rights. This note explores the matters of policy and technological culture in relation to the Act that the *ReDigi* court failed to address—essentially passing the issue to Congress.¹⁷

8. David Kravets, *Online Market for Pre-Owned Digital Music Hangs in the Balance*, WIRED, Feb. 12, 2012, <http://www.wired.com/threatlevel/2012/02/pre-owned-music-lawsuit/>.

9. *Is ReDigi Legal? Yes!*, STUDIO LEGAL CLIPEO, Nov. 3, 2013, http://www.studiolegal.com/eclipse.it/blog/wp-content/uploads/2013/03/DOCUMENTO_Is-ReDigi-Legal-Yes.pdf (no longer available at www.redigi.com).

10. Matt Peckham, *ReDigi CEO Says the Court Just Snatched Away Your Right to Resell What You Legally Own*, TIME, Apr. 25, 2013, available at <http://techland.time.com/2013/04/25/redigi-ceo-says-the-court-just-snatched-away-your-right-to-resell-what-you-legally-own/#ixzz2w3LAA9Of>.

11. *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 644–45 (S.D.N.Y. 2013).

12. *Is ReDigi Legal? Yes!*, *supra* note 9.

13. *A&M Records, Inc. v. Napster, Inc.*, 114 F. Supp. 2d 896, 927 (N.D. Cal. 2000) (holding that "defendant has contributed to illegal copying on a scale that is without precedent").

14. Bruce Houghton, *Bopaboo Used MP3 Store Walks a Legal Tight Rope*, HYPEBOT, Dec. 10, 2008, <http://www.hypebot.com/hypebot/2008/12/bopaboo-used-mp.html> (explaining how Bopaboo had no security measure or infringement detecting technology in place, allowing users to sell music files and retain a copy on their hard drive).

15. *ReDigi*, 934 F. Supp. 2d at 660.

16. *Id.* at 645 (prefacing the decision that "[b]ecause this is a court of law and not a congressional subcommittee or technology blog, the issues are narrow, technical, and purely legal").

17. *Id.*

Section II details the ReDigi technology and how the Act applies to that technology. Section III follows with a discussion of the history and development of the exclusive reproduction right and the first sale doctrine under the Act in the digital media context. This note then briefly investigates why a “digital secondary market” would benefit the music industry and maintain an equitable balance between the rights of copyright holders and consumers while illustrating a strong motivation for legislative action. Finally, Section IV discusses the relevant considerations associated with two potential legislative reforms: a “digital first sale” doctrine and a “temporary reproduction” exception to the Act. This note proposes a legislative initiative adopting a narrow “temporary reproduction” exception that permits the existence of a secondary digital market as an additional business model for the music industry that maintains an equitable balance of consumers’ and copyright holders’ rights.

II. Background

A. ReDigi: How Does It Work?

1. Overall Concept

ReDigi’s product is a cloud-based digital platform enabling peer-to-peer transactions in legally purchased music.¹⁸ When ReDigi launched its services, it promised to set itself apart from other legal and illegal digital resale alternatives for music consumers by calling itself, “the world’s first, real legal alternative to expensive online music retailers and to illegal file sharing.”¹⁹ Recognizing at an early stage that the ReDigi technology was groundbreaking and could be a cause for concern to copyright holders, the company made efforts to structure its digital marketplace in accordance with copyright law.²⁰ ReDigi emphasized how its patent-pending Verification Engine, Atomic Transaction technology, and Cloud Locker storage system functioned coherently to produce a legal, user-run marketplace that brought “physicality” to digital goods.²¹ Before applying the facts of ReDigi’s “secondary digital market” to existing law, this section will first explain the process of buying and selling content using ReDigi technology.

The first step users must take in order to sell their music through the ReDigi marketplace is to download the Media Manager tool.²² Because

18. *Is ReDigi Legal? Yes!*, *supra* note 9.

19. *Id.*

20. *Id.*

21. *Id.*

22. *ReDigi*, 934 F. Supp. 2d at 645.

ReDigi only permits users to sell “lawfully purchased”²³ content that they actually own,²⁴ the Media Manager (along with the Verification Engine) does not allow media files to be transferred to the Cloud Locker unless the file meets certain eligibility requirements.²⁵ Music files eligible for the ReDigi marketplace were limited to files purchased through iTunes, ReDigi, or from another ReDigi user.²⁶

After a user uploads the files for sale or storage,²⁷ the Media Manager continues to run on the user’s device, checking to make sure the user does not possess copies of the file that was uploaded to the Cloud Locker.²⁸ If a user transfers a file to the Cloud Locker and retains an additional copy of that file, ReDigi will suspend and eventually terminate that user’s account if the user does not comply with demands to delete the additional infringing file.²⁹

Once a file has been successfully uploaded to the Cloud Locker, the user can choose to put the file up for sale, stream the file from the Cloud Locker, or download the file back to the user’s hard drive.³⁰ When the user sells a file, that *particular* file,³¹ along with the accompanying license,³² are transferred to the purchaser upon sale.³³ The buyer and seller negotiate to agree on a price within ReDigi’s set upper and lower limits.³⁴ The Atomic Transaction technology then transfers the file to the buyer and deletes the seller’s copy of the file stored in the Cloud Locker.³⁵ ReDigi analogizes this purely digital exchange between buyer and seller to a used CD sale in a brick and mortar music store.³⁶

23. *Is ReDigi Legal? Yes!*, *supra* note 9.

24. Theodore Serra, Note, *Rebalancing at Resale: ReDigi, Royalties, and the Digital Secondary Market*, 93 B.U. L. REV. 1753, 1759 (2013) (explaining that “because of their ease of duplication and distribution, digital works are often offered to consumers pursuant to license agreements” as opposed to outright ownership).

25. *ReDigi*, 934 F. Supp. 2d at 645.

26. *Id.*

27. *See Is ReDigi Legal? Yes!*, *supra* note 9 (stating that ReDigi’s cloud service gives users the option to decide which songs files they would like to store or sell when transferring them to the cloud).

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.* (emphasis added).

32. *Id.*

33. *See ReDigi*, 934 F. Supp. 2d at 646 (illustrating how “users buy music with credits they either purchased from ReDigi or acquired from other sales”).

34. *See id.* (“ReDigi’s website prices digital music files at fifty-nine to seventy-nine cents each.”).

35. *Is ReDigi Legal? Yes!*, *supra* note 9.

36. *Id.*

2. Applying the Text of 17 U.S.C. § 106 to ReDigi

At first glance, the ReDigi marketplace does seem fairly analogous to selling a CD in a music store. So long as only one copy of the file exists before the sale, and one copy exists after the sale, the two appear functionally equivalent. But there is one key difference: ReDigi's process requires that the digital music file be *copied* to execute the transfer from the seller's hard drive to the Cloud Locker. This difference was central to the *ReDigi* litigation as perhaps the most fundamental right afforded to copyright holders under the Copyright Act is the exclusive right to "reproduce their work in copies or in phonorecords."³⁷ Whether an unauthorized duplication of a digital music file for purposes of resale constitutes copyright infringement was an issue that had not been addressed prior to the *ReDigi* case.³⁸ The *ReDigi* court ultimately held that the transfer from selling user, to Cloud Locker, to buying user, was an unauthorized duplication and thus copyright infringement.³⁹

The court broke down the ReDigi process and applied it to the text and legislative history of the Act.⁴⁰ The court also distinguished "sound recordings"—protectable copyrightable works under the statute⁴¹—from their *material objects*, or phonorecords.⁴² Applying the plain text of the statute, along with precedent established in *Matthew Bender & Co., Inc. v. W. Pub. Co.*,⁴³ the *ReDigi* court determined that "reproduction occurs when a copyrighted work is fixed in a new *material object*."⁴⁴

In applying this *material object* standard to the ReDigi process, the court looked to prior cases involving peer-to-peer file transferring. Specifically, the court looked to *London-Sire Records, Inc. v. Doe 1*, which distinguished between "copyrighted work" (digital music files) and a "material object" (the "'appropriate segment of the hard disk' that the file would be

37. 17 U.S.C. § 106 (2014).

38. *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 648 (S.D.N.Y. 2013).

39. *Id.* at 651.

40. *Is ReDigi Legal? Yes!*, *supra* note 9, at 649.

41. 17 U.S.C. § 101 (defining "sound recordings" as "works that result from the fixation of a series of musical, spoken, or other sounds . . . regardless of the nature of the material objects, such as disks, tapes, or other phonorecords, in which they are embodied").

42. *Is ReDigi Legal? Yes!*, *supra* note 9. The Copyright Act defines "phonorecords" as "material objects in which [sound recordings] are fixed by any method now known or later developed, and from which the sounds can be perceived, reproduced or otherwise communicated, either directly or with the aid of a machine or device." 17 U.S.C. § 101.

43. *ReDigi*, 934 F. Supp. 2d at 648–49 (emphasis added) (citing *Matthew Bender & Co., Inc. v. W. Pub. Co.*, 158 F.3d 693, 703 (2d Cir. 1998) (explaining that the "the relevant statutory wording refers to material objects in which 'a work' readable by technology 'is fixed.'")).

44. *ReDigi*, 934 F. Supp. 2d at 648.

embodied in following its transfer”).⁴⁵ Because a file transfer to a different *material object* requires a reproduction, the *ReDigi* court concluded that it would be “simply impossible [for] the same ‘material object’ [to be] transferred over the Internet.”⁴⁶ Thus, the court held that moving a file from one user’s computer—one material object—to the Cloud Locker—a different material object—violated Capitol’s exclusive reproduction rights.⁴⁷

Following this decision, ReDigi’s CEO John Ossenheimer explained the difference between his company’s “bit-by-bit” process of moving digital files and the “transfer and delete” process of moving digital files that the court described as ReDigi’s.⁴⁸ Both processes ultimately leave only one file remaining; however, the “bit-by-bit” process is described as moving a digital file to another location one bit⁴⁹ at a time so that multiple copies of the same particular file never contemporaneously exist. In many ways, these “bit-by-bit” transfers closely resemble a physical transfer, as they seem to require a similar “give and take” mechanism. The bit-by-bit transfer process is frequently utilized in the banking industry to ensure that money, while being digitally transferred, is never in two places at once.⁵⁰ While the bit-by-bit process minimizes the risk of additional copies when moving digital files relative to the “transfer and delete” process, the same *material object* analysis used by the *ReDigi* court can be applied to bit-by-bit transfers and would likely result in an unauthorized reproduction as well.

Because the court held that ReDigi infringed Capitol’s reproduction and distribution rights, the only legal option that remained for ReDigi was to assert fair use⁵¹ and first sale doctrine⁵² defenses. The issue of fair use in this case exceeded the application of the claim against ReDigi, drawing the attention of global technology and digital media mogul Google, Inc. (“Google”) as it pertained to the function of Google’s emerging “cloud

45. *Id.* at 649 (quoting *London-Sires Records, Inc. v. Doe 1*, 542 F. Supp. 2d 153, 166 & n.16 (D. Mass. 2008)).

46. *Is ReDigi Legal? Yes!*, *supra* note 9, at 649.

47. *Id.*

48. Peckham, *supra* note 10.

49. Bradley Mitchell, *bit*, ABOUT.COM, http://compnetworking.about.com/cs/basicnetworking/g/bldef_bit.htm (defining “bit” as the smallest unit of data transfer on a computer network”) (last visited Mar. 10, 2014).

50. Serra, *supra* note 24, at 1766.

51. See 17 U.S.C. § 107 (2014) (“Notwithstanding the provisions of sections 106 and 106A . . . the fair use of a copyrighted work, including such use by reproduction in copies or phonorecords or by any other means specified by that section, for purposes such as criticism, comment, news reporting, teaching (including multiple copies for classroom use), scholarship, or research, is not an infringement of copyright.”).

52. *Id.* § 109(a).

computing” services.⁵³ Ultimately, the court applied the four part fair use test⁵⁴ to the ReDigi process and concluded that the intermediate copying of the digital file—while temporary—was not fair use as the digital file was reproduced in its entirety and used primarily for commercial purposes.⁵⁵

The court found ReDigi’s arguments asserting the first sale affirmative defense similarly unpersuasive.⁵⁶ Under section 109 of the Act, “the owner of a particular copy or phonorecord *lawfully* made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.”⁵⁷ However, this provision—commonly known as first sale doctrine—applies as a defense to instances involving infringement of a copyright holder’s *distribution* right, not a copyright holder’s *reproduction* right. The court applied the plain language of the first sale doctrine to the ReDigi sale process and held it inapplicable because the digital purchases from ReDigi’s Cloud Locker were unauthorized digital reproductions, and thus were not “lawfully made” under section 109.⁵⁸

B. Moving Forward with ReDigi Technology and Copyright Law

The Southern District’s decision in *ReDigi*, while undoubtedly appropriate under a textualist application of section 109, ultimately hindered innovative efforts in digital music. Despite ReDigi’s good faith efforts, it fell under the umbrella of infringement due to the “Phonorecord Problem”⁵⁹—a technicality arising out of the language of the Act that expands the scope of a *material object* to any method, “now known or later developed,” that physically “fixes” a sound recording.⁶⁰ Congress’ use of the phrase “or later developed,” in describing what methods will suffice to

53. Letter Request to File an Amicus Curiae Brief of Google Inc. at 1, Capitol Records, LLC v. ReDigi Inc., 934 2d 640, No. 12-cv-0095 RJS (S.D.N.Y. 2013), available at http://beckermanlegal.com/Lawyer_Copyright_Internet_Law/capitol_redigi_120201GoogleLetterReAmicusBrief.pdf (last visited Nov. 6, 2014) (request denied by order, *ReDigi*, 934 2d 640, ECF No. 24).

54. See *Fair Use*, U.S. COPYRIGHT OFFICE, <http://www.copyright.gov/fls/fl102.html> (last visited Mar. 10, 2014) (summarizing the four part test in the doctrine as weighting (1) “[t]he purpose and character of the use;” (2) “[t]he nature of the copyrighted work;” (3) “[t]he amount and substantiality of the portion used in relation to the copyrighted work as a whole;” and (4) “[t]he effect of the use upon the potential market for, or value of, the copyrighted work”).

55. *ReDigi*, 934 F. Supp. 2d at 654.

56. *Id.* at 656.

57. 17 U.S.C. § 109(a) (emphasis added).

58. *ReDigi*, 934 F. Supp. 2d at 656.

59. Rick Sanders, *Music Industry v. ReDigi: The Problem with Phonorecords: Copyright*, AARON SANDERS PLLC, <http://www.aaronsanderslaw.com/blog/music-industry-v-redigi-the-problem-with-phonorecords-copyright/> (coining and defining, the “phonorecord problem”) (last visited Mar. 10, 2014).

60. See 17 U.S.C. § 101.

be a material object in section 101 of the Act seems to be a safeguard against technologies that did not exist, or were not even in contemplation, in 1978 when that portion of the statute was enacted.⁶¹

Given the myriad technological advancements in media consumption that have in many ways defined the previous two or three decades, the Act is long overdue for corresponding breakthroughs of its own. In fact, one scholar went as far as urging Congress to create an updated version of the Act that is more in sync with the booming digital media culture, called the Next Great Copyright Act.⁶²

III. Analysis

A. The Call for the Next Great Copyright Act

While this note focuses on potential legislative reform regarding the particular statutory definitions encompassing the result of the ReDigi case, Register of Copyrights, Maria Pallante, recently urged Congress to adopt a more general revision of the statute given the various technological changes surrounding copyright and commerce.⁶³ Pallante stressed that it had been fifteen years since Congress “acted expansively in the copyright space,” and that the time had come for another “visible and far-reaching” amendment to copyright law.⁶⁴ While Pallante recommended Congress take broad action, as opposed to enacting smaller amendments over a longer timeline, some specific recommendations to be considered for her suggested general revision included aspects of copyright law that were seminal points in the ReDigi decision.⁶⁵ For example, Pallante specifically sought Congressional attention for “clarifying the scope of exclusive rights,” “exempting incidental copies in appropriate instances,” and perhaps most significant, “reforming the music marketplace.”⁶⁶

Some copyright scholars who agree with the ReDigi court’s textualist approach may claim that Pallante’s reform requests were not suggested with ReDigi in mind. For example, one may argue that Pallante’s statement was published ten days⁶⁷ prior to the ReDigi decision and that

61. *Id.*

62. See generally Maria Pallante, *The Next Great Copyright Act*, 36 COLUM. J.L. & ARTS 315 (2013).

63. *The Register’s Call for Updates to U.S. Copyright Law Before the Subcommittee on Courts, Intellectual Property, and the Internet of the Committee on the Judiciary House of Representatives*, 113th Cong. 6–8 (2013), http://www.copyright.gov/docs/hearing_testimony.pdf.

64. *Id.*

65. *Id.*

66. *Id.*

67. *Id.* at 315; see also *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 640 (S.D.N.Y. 2013).

she fails to mention “ReDigi” in either of her publications regarding the Next Great Copyright Act (the Committee on the Judiciary Hearing in the House of Representatives,⁶⁸ or her article published in the *Columbia Journal of Law and Arts*⁶⁹). However, a number of opponents to the strict textual approach of the ReDigi court have expressed, similar to Pallante, a need for amendment specific to the ReDigi litigation.

For instance, when analyzing ReDigi’s failed attempt to avoid the “reproduction hurdle”⁷⁰ in his Note published in the *Boston University Law review*, Theodore Serra suggests generally that an allowance of intermediate copying for technologies like ReDigi’s is a necessity for a digital secondary marketplace to exist.⁷¹ Additionally, the treatise, *Nimmer on Copyright*, suggests that as the first sale doctrine of the Act stands today, there is no real likelihood of adequately applying a digital first sale defense in the context of a digital secondary market without either amendment, or perhaps future technologies that can ascertain a way to side-step the reproduction stage in a digital sale.⁷² While the topic of potential amendments to the Act in the emergence of digital media has been ripe for discussion both before and immediately after the ReDigi decision, a more detailed analysis of the history and nuances of the reproduction right and first sale doctrine is necessary to adequately propose legislative reform that would enable secondary digital music market.

B. Copyright Holder’s Exclusive Right to Reproduction

1. Digital Reproduction Rights: A Brief History

The owner of a copyright in a sound recording generally has the exclusive right—subject to some statutory exceptions—to “reproduce the copyrighted work in copies or phonorecords.”⁷³ Under section 114(b) of the Act, the reproduction right in copyrights of sound recordings is “limited to the right to duplicate the sound recording in the form of phonorecords or copies that directly or indirectly recapture the actual sounds fixed in the recording.”⁷⁴ The advent of digital music—and the corresponding opportunities for infringement—dramatically altered the landscape surrounding reproduction rights in music copyright. Unlike previous

68. See Pallante, *supra* note 62.

69. *Id.*

70. Serra, *supra* note 24, at 1763–66.

71. *Id.* at 1766.

72. 2-8 *Nimmer on Copyright* § 8.12(E).

73. 17 U.S.C. § 106(1) (2014).

74. *Id.* § 114(b).

mediums of fixation, such as vinyl records and CDs, digital music files are very easy to copy and transfer.

In 1987, the Moving Pictures Experts Group set a standard file format for storing audio recordings in digital form—known famously as “MP3.”⁷⁵ An MP3 file is created using a software process called “ripping,” where a computer user can condense audio information (that is, sound recordings) taken from a compact disc into a smaller format, which can then be stored on the user’s hard drive.⁷⁶ In MP3 form, music files behave much like other computer files—making copies is attainable through merely two or three mouse clicks. Ease of reproduction and network connectivity thus permit the transfer of these music files in a rapid fashion, and the result is ostensibly a recipe for mass infringement. The legality of this “compressing,” downloading, and distributing of MP3 music files in regards to a copyright holder’s exclusive reproduction right is detailed in the *Napster* line of digital music cases.

Not surprisingly, online platforms for MP3 “file sharing” emerged relatively shortly after the MP3 format itself. Both the Ninth Circuit of the United States Court of Appeals (in *Napster*) and the United States District Court of the Southern District of New York (in *UMG*)⁷⁷ were swift in recognizing that users of MP3 storage and sharing sites were directly infringing a copyright holder’s exclusive reproduction right by uploading the audio information from CDs to their hard drives.⁷⁸ While the courts, and even major record labels,⁷⁹ have conceded that a consumer who uploads songs from purchased CDs to an MP3 format on his or her hard drive may escape infringement of the reproduction right through the defense of fair use if the MP3 is strictly for personal use,⁸⁰ sites like Napster and MP3.com did not limit users to “personal use” of the digital files uploaded to the site.⁸¹ These sites’ main function was to exploit the mass amounts of newly available digital music by permitting users to download, from any other user’s MP3 library, files that typically were not originally purchased either as a CD or in a legitimate MP3 transaction.⁸²

75. *A&M Records, Inc. v. Napster, Inc.*, 114 F. Supp. 2d 896, 901 (N.D. Cal. 2000).

76. *Id.*

77. *UMG Recordings v. MP3.com, Inc.*, 92 F. Supp. 2d 349 (S.D.N.Y. 2000).

78. *See Napster*, 114 F. Supp. 2d at 927; *see also Umg Recordings*, 92 F. Supp. 2d at 353.

79. *The Law*, Recording Industry Association of America, http://www.riaa.com/physical_piracy.php?content_selector=piracy_online_the_law (last visited Mar. 10, 2014).

80. *Id.*

81. *See Napster*, 114 F. Supp. 2d at 901–05 (explaining how a Napster user may upload a legally purchased CD to his or her hard drive, which then makes that CD accessible to every Napster user for free via the file sharing process).

82. For example, if one user were to legally purchase a song by Eminem—an internationally famous rap musician that rose to fame around the time Napster’s services became popular—every

Because Internet users were able to digitally acquire illegal music so easily, massive service providers (such as Napster) would *only* be able to continue operating by incorporating copyright protection measures in compliance with the Digital Millennium Copyright Act.⁸³ Such measures must enable the service provider to recognize when users are uploading infringing content and remove the content from the site so additional users cannot download that content.⁸⁴

While the source of digital files uploaded by ReDigi users is predominately an iTunes library rather than a CD, the digital reproduction is virtually identical to Napster and MP3.com in regards to how the file moves from one location (the user's hard drive) to another (ReDigi Cloud Locker). Recognizing this broad similarity between these two otherwise different services, it was critical for ReDigi to distinguish its services from the infamous Napster and other peer-to-peer sharing services. Ultimately, ReDigi set itself apart from anti-copyright digital media platforms operating illegally prior to ReDigi through its policy to use only secure and lawfully purchased digital files (from iTunes, ReDigi, or ReDigi users), its further detection and takedown measures of infringing files that may make it on the server, and its calculated stream of royalty payments to copyright holders.

Falling on the spectrum of online services somewhere between Napster and ReDigi, a company called Bopaboo was actually the first to offer an online marketplace for audio files.⁸⁵ Several aspects of the Bopaboo service contributed to the company's short life: (1) no "bit-by-bit" or "transfer and delete" function occurred during uploading, which permitted a user to sell an MP3, retain a separate copy on his or her hard drive (post-sale), and even resell that additional copy "seconds later";⁸⁶ (2) Digital Rights Management protections were not in place to detect whether illegally reproduced MP3s were being uploaded and sold;⁸⁷ (3) songs were often sold at lower than half the value of the original purchasing price (or, in many cases, there was no original purchasing price due to the sale of

Napster user searching for that song would then have the opportunity to download it from the initial uploading user or other subsequent uploading users.

83. See 17 U.S.C.S § 512 (2014).

84. *Id.* § 512(c)(1)(A) (explaining that an Internet service provider (ISP) shall not be liable for user-uploaded infringing content provided that the ISP: (1) "does not have actual knowledge that the material or an activity using the material on the system or network is infringing;" (2) "in the absence of such actual knowledge, is not aware of facts or circumstances from which infringing activity is apparent;" or (3) "upon obtaining such knowledge or awareness, acts expeditiously to remove, or disable access to, the material.").

85. Houghton, *supra* note 14.

86. *Id.*

87. *Id.*

infringing files);⁸⁸ and (4) and no resale royalty was distributed to copyright holders.⁸⁹ While Bopaboo initially advertised its service as legal, many record labels and the Recording Industry Association of America disagreed and refused to sit back while Bopaboo continued its services without dispersing sufficient royalty revenues.⁹⁰

Although ReDigi made serious efforts to conform with digital media policy considerations illustrated in the *Napster* case and with the Bopaboo issue,⁹¹ the largest obstacle for ReDigi was getting over the “reproduction hurdle” during the upload process. The reproduction hurdle is a direct result of the “Phonorecord Problem”⁹² created through overbroad statutory language in the Act. Although ReDigi’s service creates a “de facto” physical copy upon transferring a digital file to the Cloud Locker and deleting the file on the user’s hard drive, the failure to get over the “reproduction hurdle” reduces ReDigi from an innovator to an infringer in the eyes of copyright law. Thus, so long as the technology involves making a “reproduction,” secondary digital music markets like ReDigi’s are effectively prohibited under copyright law. If adopted, however, a limited statutory exception permitting a temporary, transitory reproduction would enable services like ReDigi to provide a lawful platform for reselling digital music. This concept is not new to copyright law and has been given serious consideration—even resulting in legislative action—in light of various technological advancements creating a clash of law and policy similar to ReDigi.

2. Relevant Amendment Efforts Regarding Digital Media

Two decades prior to ReDigi, the problem of the “reproduction hurdle” and the need for incidental copying came to light in the computer repair industry. In *MAI Systems Corp. v. Peak Computer*, the Ninth Circuit held that “the loading of software into [a computer’s Random Access Memory (“RAM”)] creates a copy under the Copyright Act.”⁹³ Peak—a computer repair company with nearly seventy percent of its clients using MAI computers and software—argued that such loading of software was not “fixed”—as required to constitute a “copy” under the Act⁹⁴—and was a

88. *Id.*

89. Scott Kirsner, *Can ReDigi, New Marketplace for ‘Used’ Digital Music, Avoid Lawsuits and Prosper?*, BOSTON.COM, Oct. 5, 2011, http://www.boston.com/business/technology/innoeco/2011/10/can_redigi_new_marketplace_for.html (last visited Mar. 10, 2014).

90. *Id.*

91. *Is ReDigi Legal? Yes!*, *supra* note 9.

92. *See Sanders, supra* note 59.

93. *MAI Sys. Corp. v. Peak Computer*, 991 F.2d 511, 513 (9th Cir. 1993).

94. *Id.* at 517–18.

necessary step in servicing clients' computers.⁹⁵ Notwithstanding the necessary and transitory nature of the software "copies" by Peak, the court held that such copying violated MAI's reproduction right under the Act.⁹⁶

Despite a white paper from the Clinton Administration favoring the decision of the Ninth Circuit in *MAI Systems Corp.*, Congress felt that computer repair companies like Peak should not be punished for making necessary, temporary reproductions of copyrighted computer programs in order to service client computers.⁹⁷ Congress amended the Act by "adding an exception to § 117 to allow computer repair technicians to make [temporary] RAM copies" without implicating a copyright holder's right to reproduction.⁹⁸ Thus, Congress created a carve-out for temporary reproductions in the computer repair context enabling companies such as Peak to overcome the "reproduction hurdle."

While the computer repair exception added to section 117 following the *MAI Systems Corp.* decision is the only carve-out Congress created for temporary reproductions in the digital context, talk of other exceptions existed even before enactment of this exception.⁹⁹ In fact, some commentators have gone as far as claiming that the "promotion and growth of electronic commerce requires a general exception for temporary incidental copies to cover all forms of digital content, not just computer software."¹⁰⁰ This "general exception" is likely over inclusive. Moreover, as part of the *ReDigi* decision indicated, there are still specific situations in which temporary copying is protected under fair use. For example, as discussed in Section II.A.2,¹⁰¹ Google clearly had a significant stake in the *ReDigi* litigation, as a favorable ruling on the permissibility of temporary copying from a hard drive to a cloud server would ease its concerns with respect to cloud computing.¹⁰² The "cloud computing" aspect that Google is concerned with involves users' ability, "at their own discretion, to move or copy their digitally owned files," which is a primary function of cloud computing—a \$41 billion industry.¹⁰³ The *ReDigi* court held that fair use

95. *Id.* at 518.

96. *Id.* at 518–19.

97. Serra, *supra* note 24, at 1764.

98. *Id.*

99. *DMCA Section 104 Report*, U.S. COPYRIGHT OFFICE, 53–54 (Aug. 2001) available at <http://www.copyright.gov/reports/studies/dmca/sec-104-report-vol-1.pdf>.

100. *Id.*

101. See Letter Request to File an Amicus Curiae Brief of Google Inc, *supra* note 53.

102. *Id.*

103. Mark Fidelman, *BREAKING: Google to Capitol Records—We're Not Going to Let You Shut Down Cloud Computing*, SEEK OMEGA (Feb. 2, 2012), <http://www.seekomega.com/2012/02/breaking-google-to-capitol-recordswere-not-going-to-let-you-shut-down-cloud-computing/> (last visited Mar. 10, 2014).

did not apply to the ReDigi services,¹⁰⁴ but did not expressly state that it would not apply to the reproduction involved with transferring a music file from a user's hard drive to the Cloud Locker merely for personal use, as opposed to resale purposes. While clear answers regarding the application of fair use to cloud computing services have yet to be provided,¹⁰⁵ fair use advocates feel strongly that cloud computing services permitting users to reproduce their own licensed content solely for personal use can avoid the temporary reproduction infringement through fair use.¹⁰⁶

Given that cloud computing services facilitating the temporary reproduction of digital music files for storage and personal uses are more likely to be protected under fair use, a far-reaching "general exception" for temporary reproductions across all digital media technologies seems to be unnecessary. However, based on the *ReDigi* court's purely textual approach to the issue and dissatisfaction with *ReDigi*'s fair use argument,¹⁰⁷ fair use will likely never be a defense for necessary, temporary reproductions "incident to a sale"¹⁰⁸ in secondary digital music market platforms—absent some change in circumstance. In the future, even if companies like *ReDigi* were able to overcome the "reproduction hurdle," the copyright holder's distribution right may also be infringed unless a "digital" first sale defense can be utilized by consumers.

C. The Consumer's First Sale Rights

1. Brief History in the Digital Media Context

Section 109 of the Copyright Act ratifies the Supreme Court of the United States' decision in *Bobbs-Merrill Co. v. Straus*, where the "first sale" exception to a copyright holder's exclusive right to distribution was created.¹⁰⁹ Section 109 (the "first sale doctrine") reads: "Notwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord *lawfully made* under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord."¹¹⁰

104. See *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 654 (S.D.N.Y. 2013).

105. Dr. Matthew Rimmer, *Dr. Matthew Rimmer Takes a Closer Look at Fair Use*, TECHDIRT (Feb. 1, 2014), <https://www.techdirt.com/articles/20140131/16224426064/dr-matthew-rimmer-takes-closer-look-fair-use.shtml>.

106. See Geoffrey Manne, Ryan Radia & Ben Sperry, *A Supreme Court Ruling Against Aereo Won't Spell the End of Cloud Computing*, TRUTH ON THE MARKET (Apr. 17, 2014), <http://truthonthemarket.com/2014/04/17/a-supreme-court-ruling-for-aereo-wont-spell-the-end-of-cloud-computing/>.

107. See *ReDigi*, 934 F. Supp. 2d at 645, 654.

108. *Id.*

109. *DMCA Section 104 Report*, *supra* note 99, at 20.

110. 17 U.S.C. § 109 (2014) (emphasis added).

Traditionally, this exception was reserved for the resale of *physical goods*,¹¹¹ such as books, CDs, cassette tapes and DVDs (to name a few). The rapid growth of digital media, however, stimulated efforts to move towards a *digital* first sale defense as well.¹¹²

It is important to note the distinction between a “digital first sale” statutory exception, and applying the “first sale doctrine”—as it stands today—to physical copies of works in *digital format*. The U.S. Copyright Office’s DMCA Section 104 Report (the “Report”) clearly speaks to this distinction, saying that section 109 does apply to digital content and that “[p]hysical copies of works in a digital format, such as CDs or DVDs, are subject to section 109 in the *same way as physical copies* of works in analog form.”¹¹³ Thus, a “lawfully made tangible copy of a digitally downloaded work” may be lawfully sold under the first sale doctrine.¹¹⁴ The problem for ReDigi, however, was that the technology required the music files be “copied” as part of the upload process.¹¹⁵ Thus, buyers in ReDigi’s marketplace receive a “new copy,” and not the “same one with which the sender began,” as originally intended under first sale doctrine.¹¹⁶

While the Report provided great insight into the potential existence and effects of a digital first sale doctrine, the report ultimately recommended against amending the Act to facilitate a digital first sale.¹¹⁷ This recommendation was largely based on the Copyright Office’s determination that physical and digital copies had too many distinguishing characteristics to be determined legal equivalents under copyright law.¹¹⁸ The Report acknowledged that a “transfer and delete” process is very similar to a physical transaction in so far as the transaction involves only one copy.¹¹⁹ It went on, however, to point out that the problem lies in the circulation of these “used” digital goods compared to “used” physical goods; specifically, the latter will inevitably be subject to physical wear and tear while the former will not and can be circulated throughout the market essentially indefinitely.¹²⁰

The Report’s analysis in the “digital first sale” context, as well as in other areas of digital copyright law, received deference from courts in

111. *ReDigi*, 934 F. Supp. 2d at 655–56.

112. *DMCA Section 104 Report*, *supra* note 99, at 78.

113. *Id.* (emphasis added).

114. *Id.*

115. *Id.* at 79.

116. *Id.*

117. *Id.* at 97; *see also* 2-8 Nimmer on Copyright § 8.12(E), n.279.

118. *DMCA Section 104 Report*, *supra* note 99 at 81–86.

119. *Id.* at 81–82.

120. *Id.*

various decisions. For example, in *Cartoon Network LP v. CSC Holdings, Inc.* (a digital media case regarding whether the acts of “buffering” in the operation of a RS-DVR is considered “reproduction”),¹²¹ the Second Circuit held that the findings and position of the Report was entitled to legislative deference¹²² under *Skidmore v. Swift & Co.* This means the report was given the “power to persuade” the court.¹²³ Although the results in the Report did not persuade the Second Circuit in *Cartoon Network*, the *ReDigi* court recognized the level of deference given to the report and held that the analysis of the digital first sale doctrine was sufficiently persuasive in that the exception should not apply to *ReDigi*.¹²⁴

It is clear that the *ReDigi* court rejected the application of a “digital first sale” defense based on the plain text of the statute despite *ReDigi*’s argument that technological changes have rendered the text ambiguous and require the court to construe the Act in light of its basic purpose: to “incentivize creative work . . . [and] promot[e] broad public availability of . . . music . . .”¹²⁵ In a final note on the first sale aspect of the case, the court explains that the policy concerns of the “digital first sale” exception are “left to Congress, and not this court.”¹²⁶ Thus, as digital media continues to grow, there seem to be two starkly contrasting views as to how Congress should treat the first sale doctrine moving forward: one view is that “section 109 should be amended to permit the digital transmission of works that were lawfully acquired (including the reproduction of the work as a part of the transmission process), and the other oppos[es] modification of section 109.”¹²⁷ The former view is clearly beneficial for consumers of digital music, while the latter view favors copyright holders. A further look into the various legislative efforts in regards to a “digital first sale” exception will prove helpful in determining what the best recommendation will be moving forward.

2. Relevant Amendment Efforts Regarding Digital First Sale

Despite the recent media attention to the *ReDigi* litigation’s implications for reproduction rights and the first sale defense in the digital context, the most powerful legislative efforts regarding a “digital first sale”

121. *Cartoon Network LP, LLLP v. CSC Holdings, Inc.*, 536 F.3d 121, 127 (2008).

122. *Id.*

123. *Id.*

124. *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 656 (S.D.N.Y. 2013).

125. *Id.* at 655 (quoting *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 156 (1975)).

126. *Id.*

127. *DMCA Section 104 Report*, *supra* note 99, at 44.

doctrine occurred in 2003.¹²⁸ Given that there is still dispute as to whether a “digital first sale” exception should exist, it is clear that none of the three Bills introduced in 2003¹²⁹ were enacted into law. However, it is important to note that while the proposed legislation for a “digital first sale” failed before, the ReDigi platform for resale of digital music files was merely a speculation in 2003, whereas now, secondary digital market technology can clearly be implemented.

The first proposed piece of legislation, Senate Bill 692, was directed towards “first sale” of digital content, and did not propose a separate “digital first sale” defense.¹³⁰ The bill would have required producers of digital content to “disclose the nature of restrictions that limit the practical ability of the content purchaser to play, copy, transmit, or *transfer* such content on, to, or between devices commonly used with respect to that type of content.”¹³¹ Unlike Senate Bill 692, the other proposed pieces of legislation—House Bill 1066 and Senate Bill 1621—were specifically aimed at “expanding the first sale exception to incorporate digital works.”¹³²

The “Findings” portion of Senate Bill 1621 stated that, “it is not in the interests of our Nation’s economy . . . to permit the advent of access or redistribution control technologies to limit the existence of legitimate secondary markets for digital media products.”¹³³ And further, this “traditional form of commerce . . . is founded in our Nation’s economic traditions,” and “provides critical resources.”¹³⁴ The bill ultimately proposed to amend the first sale doctrine to provide: “The lawful owner of a digital media product may transmit a copy of that product by means of a transmission to a single recipient as long as the technology used by that person to transmit the copy *automatically deletes* the digital media product contemporaneously with transmitting the copy.”¹³⁵ If the bill had been enacted, ReDigi’s technology would have complied with the proposed digital first sale doctrine, and thus would have been able to avoid infringement liability.

House Bill 1066 was similar to Senate Bill 1621 in that it proposed an actual “digital first sale” exception. However, it was the only “digital first sale” proposed legislation that sought an amendment to section 109 of the

128. Serra, *supra* note 24, at 1785.

129. See *infra* note 132.

130. *Id.*

131. S. 692, 108th Cong. § 3 (2003) (emphasis added).

132. Serra, *supra* note 24, at 1782.

133. S. 1621, 108th Cong. § 2(8) (2003).

134. *Id.*

135. *Id.* at § 5 (emphasis added).

Act “as opposed to adding a separate provision.”¹³⁶ According to the bill’s drafters, the “development of digital technology and the rise of the Internet have once again altered the balance” of copyright holders and consumers.¹³⁷ Thus, House Bill 1066 would have modified first sale doctrine such that the defense would be applicable to:

case[s] in which the owner of a particular copy or phonorecord of a work in a digital or other non-analog format, or any person authorized by such owner, sells or otherwise disposes of the work by means of a transmission to a single recipient, if the owner does not retain the copy or phonorecord in a retrievable form and the work is so sold or otherwise disposed of in its original format.¹³⁸

While the two digital first sale bills sound very similar, Senate Bill 1621 required an automatic “transfer and delete” process whereas House Bill 1066 required that the seller retain no copy of the sold content.¹³⁹ Even with a more balanced support through bipartisanship in House Bill 1066,¹⁴⁰ the proposed legislation also was introduced to a committee in 2003 and never enacted.¹⁴¹

Despite Congressional failure to enact any “digital first sale” legislation in 2003, Judge Sullivan’s passing the issue to Congress in the *ReDigi* decision¹⁴²—along with digital media content moguls’ (Apple and Amazon’s) recent interest in patents on secondary digital market technology¹⁴³—may ignite another Congressional discussion of a digital first sale amendment. To survive the legislative gauntlet, however, any such amendment will undoubtedly require careful drafting. Fundamentally, a successful digital first sale amendment will ensure that the economics of the resulting secondary digital market strike an efficient balance between consumers’ interests and copyright holders’ interests—and it must do so in a way that

136. Serra, *supra* note 24, at 1783.

137. H.R. 1066, 108th Cong. § 4 (2003).

138. *Id.*

139. Compare S. 1621, 108th Cong. § 5 (2003), with H.R. 1066, 108th Cong. § 4 (2003); see also Serra, *supra* note 24, at 1783.

140. *Id.* at 1783.

141. H.R.1066 – Net Consumer Expectations (BALANCE) Act of 2003, CONGRESS.GOV, <http://www.congress.gov> (search “H.R. 1066” using the filter “All Legislation”; then follow the “H.R. 1066” hyperlink for the “108th Cong.”; then follow “Actions” hyperlink) (last visited Mar. 10, 2014).

142. See Serra, *supra* note 24, at 1785.

143. Andrew Albanese & Judith Rosen, *In ReDigi Case, Court Forcefully Rejects Digital First Sale*, PUBLISHER WEEKLY (Apr. 2, 2013), <http://www.publishersweekly.com/pw/by-topic/digital/copyright/article/56632-in-redigi-case-court-rejects-digital-first-sale.html> (last visited Mar. 10, 2014).

also serves the basic principles of copyright.¹⁴⁴ A further look into the potential benefits of a secondary digital music market will be useful in finding a narrowly tailored amendment that creates such a market in line the purpose of copyright laws.

D. Necessary Considerations of a Secondary Digital Market

1. *Can Digital Really Be Considered Physical?*

The differentiating characteristics between physical and digital content has emerged as a common theme in the digital copyright conversation. This distinction is important not only as a rhetorical device that highlights the clash between “the old” copyright world and “the new,” but also in so far as it may shed light on how a secondary market for digital music could impact the music industry.

Perhaps the most obvious difference between digital and physical content is the possibility of degradation associated with physical copies.¹⁴⁵ This trait alone brings to light other differences between the two in an open resale market. First, because of the potential longevity of a digital music file, the “used” file can compete just as easily, if not better (assuming its lower price), with a “new” music file. Thus, the “used” and the “new” digital content may be seen as equally desirable.¹⁴⁶ In the digital resale world, the DMCA Section 104 Report states that “[t]ime, space, effort, and cost no longer act as barriers” in a digital market due to the durability and “instantaneous” transmission of digital content.¹⁴⁷

Another significant concern is that with a physical sale, the actual “item” leaves with the buyer.¹⁴⁸ In a digital sale, this process can be mimicked with “bit-by-bit” transfers or a “transfer and delete” process, though perhaps without the same level of certainty that there has been an actual exchange of the *particular* “item.”¹⁴⁹ ReDigi’s process (Verification Engine and Atomic Transaction technology),¹⁵⁰ however, shows that there are certain technological security measures that can significantly mitigate

144. *Sony Corp. v. Universal City Studios, Inc.*, 464 U.S. 417, 429 (1984) (describing copyright as a “difficult balance between the interests of authors . . . in the control and exploitation of their writings . . . on the one hand, and society’s competing interest in the free flow of ideas, information, and commerce on the other hand”).

145. *DMCA Section 104 Report*, *supra* note 99, at 82.

146. *Id.*

147. *Id.*

148. *Id.* at 83–84.

149. *Id.* at 81–82.

150. *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 645 (S.D.N.Y. 2013) (explaining ReDigi’s technological security measures used in attempting to create a de facto physical sale).

concerns regarding retained seller copies in digital sales—a pivotal concern of the Copyright Office in the DMCA Section 104 Report. The Copyright Office feared that these technological measures “can be hacked,” and further that the cost of implementation will negatively impact the market if such costs are passed on to consumers.¹⁵¹ But perhaps now, eleven years later, the Copyright Office has a different perspective on these technologies, since: (1) there was no evidence pertaining to any deficiencies in ReDigi’s Verification Engine and Atomic Transaction technology in the *ReDigi* litigation;¹⁵² and (2) Maria Pallante (Register of Copyrights) has called for strong legislative change to the digital marketplace.¹⁵³

2. Adding the Market for Digital Streaming and Piracy to the Equation

A significant “thorn in the side” of the pro-digital resale market argument has been the distinguishing qualities between digital and physical content. The DMCA Section 104 Report pointed out that these distinguishing qualities could have a “detrimental effect” on the digital content market if “used” digital content were permitted to be resold.¹⁵⁴ However, there are two significant aspects of the digital music industry—digital streaming and digital piracy—that negatively impact outright music *purchases* that a digital resale market can potentially offset. Recent numbers show that music streaming is at an all-time high as of 2013.¹⁵⁵ And although there is dispute over *the extent* to which digital music piracy affects digital music sales, there is little dispute that it *does* affect digital music sales.¹⁵⁶

In digital streaming, there are effectively two types of services that dominate the end-user markets: “non-interactive” online radio streaming (e.g., Pandora, Sirius XM, and Live365) and user “interactive” streaming (e.g., Spotify Premium, Rhapsody, and MySpace).¹⁵⁷ The former typically provides free membership for listeners because it offers limited control over the songs that are played,¹⁵⁸ while interactive streaming services typically require paid subscriptions as users can choose from a buffet of

151. *DMCA Section 104 Report*, *supra* note 99 at 84.

152. *See generally ReDigi Inc.*, 934 F. Supp. 2d 640.

153. Pallante, *supra* note 62, at 344.

154. *DMCA Section 104 Report*, *supra* note 99 at 81–82.

155. Pfanner, *supra* note 4.

156. Michelle Catalano, *Music Piracy: Major Studies Conflicted Over Recording Industry Impact*, FORBES, Mar. 25, 2013, available at <http://www.forbes.com/sites/michelecatalano/2013/03/25/music-piracy-major-studies-conflicted-over-recording-industry-impact/> (last visited Mar. 10, 2014).

157. Thompson, *Music and How the Money Flows*, *supra* note 6.

158. *Skip Limit*, PANDORA, <http://help.pandora.com/customer/portal/articles/24601-skip-limit> (“Free Pandora accounts permit 6 skips per hour per station, for up to 24 total skips per day across all stations.”) (last visited Mar. 10, 2014).

songs offered in the service's digital library.¹⁵⁹ Non-interactive radio streaming services earn most of their revenue from advertisements, and pay compulsory royalties to publishers and copyright holders with part of that revenue.¹⁶⁰ Interactive streaming sites often pay higher negotiated royalties,¹⁶¹ as their on-demand format is essentially an alternative to the traditional method of purchasing and "owning" music. Notwithstanding the differences in revenue models, interactive and non-interactive streaming sites performed very well in 2013, touting a growth rate of 32% while overall music sales suffered a 6.3% decrease.¹⁶² In fact, there was reported to be "more than 118 billion streams in 2013[,] . . . which is the approximate revenue equivalent of 59 million albums purchased."¹⁶³ It is quite evident from these statistics, as well as major copyright holders' and their advocates' willingness to work inside the streaming business model,¹⁶⁴ that digital streaming is on the rise minimizing revenue created from digital sales.

Another drain on digital music sales—and any other form of digital media—is piracy. While the effect of piracy on the digital music industry is not as clear-cut as one might think,¹⁶⁵ what is clear is that "[i]n the decade since peer-to-peer file-sharing site Napster emerged in 1999, music sales in the U.S. . . . dropped 47 percent" (from \$14.6 billion to \$7.7 billion).¹⁶⁶ Further, only "37 percent of music acquired by U.S. consumers in 2009 was paid for," and it was recently estimated that "U.S. Internet users annually consume between \$7 [billion] and \$20 billion worth of digitally pirated recorded music."¹⁶⁷ Despite these statistics, some scholars claim there is evidence that digital music piracy is actually leading to a "slight

159. *Spotify Explained*, SPOTIFY, <https://www.spotifyartists.com/spotify-explained/> ("Spotify's Premium tier gives users unlimited music across all of their devices including smartphones, tablets and TVs . . . [and] [t]his tier costs \$9.99 per month.") (last visited Mar. 10, 2014).

160. *Id.* ("Advertisers pay Spotify for exposure to users on our free tiers and in-turn fund the royalties that Spotify pays out for listening that occurs in these tiers.").

161. *Major Music Industry Groups Announce Breakthrough Agreement*, RECORDING INDUS. ASS'N OF AM., <http://www.riaa.com/newsitem.php?id=C9C68054-D272-0D33-6EDB-DF08022C7E3A> (explaining that "mechanical royalty of 10.5% of revenue"); see also *Spotify Explained*, *supra* note 159 (explaining that "around 70% of monthly revenue is paid out to rights holders.").

162. Zack O'Malley-Greenburg, *Digital Music Sales Drop for First Time as Streaming Soars*, FORBES, Jan. 9, 2014, available at <http://www.forbes.com/sites/zackomalleygreenburg/2014/01/09/digital-music-sales-drop-for-first-time-as-streaming-soars/>.

163. *Id.*

164. See *Major Music Industry Groups Announce Breakthrough Agreement*, *supra* note 161.

165. See generally Catalano, *supra* note 156.

166. *For Students Doing Reports*, RECORDING INDUS. ASS'N OF AM., <http://www.riaa.com/faq.php> (last visited Mar. 10, 2014).

167. *Id.*

increase” in digital music sales.¹⁶⁸ The European Union conducted a “clickstream study” on Internet users and found that visits to illegal downloading sites actually did subsequently lead users to legitimate music purchasing sites.¹⁶⁹ These kinds of statistics are used to support the theory that many Internet users are beginning to use illegal downloading to “test” a song or album before purchasing it legally.¹⁷⁰ However, even if some honorable music pirates use illegal downloads solely to test-drive an album or song, there remains a considerable amount of evidence indicating that piracy negatively impacts digital music sales.

IV. Proposal

Given the digital music industry’s demonstrated willingness to change over the last decade, Copyright Act reform is perhaps a likely event in the near future. Moreover, one of the most influential figures in copyright law, Maria Pallante, has explicitly called for significant change that is consistent with the culture and economics of digital media.¹⁷¹ And since at least some amount of reform seems inevitable, the question becomes where these changes should take place.

In regards to a digital resale market, ReDigi has undoubtedly sparked an interest that has left the most powerful digital media players (e.g., Apple and Amazon) hungry to pounce on a potentially fruitful opportunity. Both Apple and Amazon took rapid steps post-*ReDigi* to secure patents involving digital media resale technology.¹⁷² These industry leaders would not need to pass a “reproduction hurdle” or first sale barrier such as in *ReDigi* because the Apple and Amazon digital resale patents only permit users to buy and sell digital content that is entirely “cloud” based—which means there would be no need to “reproduce” a copy from a user’s hard drive.¹⁷³ Unlike Apple or Amazon, a “transfer and delete” or “bit-by-bit”

168. See Catalano, *supra* note 156 (“a 10% increase in clicks on illegal downloading websites leads to a 0.2% increase in clicks on legal purchases websites,” citing Luis Aguiar & Bertin Martins, *Digital Music Consumption on the Internet: Evidence from Clickstream Data*, JRC Technical Reports, 1 (2013)).

169. Luis Aguiar & Bertin Martins, *Digital Music Consumption on the Internet: Evidence from Clickstream Data*, JRC TECHNICAL REPORTS, 1 (2013).

170. Catalano, *supra* note 156.

171. Pallante, *supra* note 62.

172. Albanese & Rosen, *supra* note 143.

173. John T. Soma & Michael K. Kugler, *Why Rent When You Can Own? How ReDigi, Apple, and Amazon Will Use the Cloud and the Digital First Sale Doctrine to Resell Music, E-Books, Games, and Movies*, 15 N.C. J.L. & TECH. 425, 449–54 (2014) (explaining the difference between the *ReDigi* digital resale process and the digital resale technology patents by Apple and Amazon. Specifically, the Amazon and Apple patents, while different, both do not permit a user to sell digital content that has been removed from “cloud” storage and placed on a user’s hard

digital resale system (which leaves consumers more autonomy with purchased content than an entirely cloud-based system) will never be able to exist without some legislative accommodation on the “reproduction hurdle” or first sale doctrine. An amendment to the Act creating a “temporary reproduction” exception or “digital first sale” defense for purposes of transactions in secondary digital music markets can both—with proper limitations—enhance the digital music industry while maintaining the foundational balance of interests in copyright law. However, a “temporary reproduction” exception is likely a more appropriate option than a “digital first sale” defense.

A central reason for supporting the “temporary reproduction” exception as opposed to creating a “digital first sale” defense is that a “digital first sale” defense has already been addressed numerous times by Congress.¹⁷⁴ Perhaps with the influence of Maria Pallante, urging Congress to take a step back and rethink copyright in the digital media context, Congress would be willing to take another serious look at the “digital first sale” concept. However, Congress could potentially address both issues while explicitly addressing only one if more attention was given to permitting a temporary reproduction exception in a secondary digital music market. If a temporary reproduction exception allowed consumers to upload files from a hard drive to a protected cloud service for later sale, the first sale defense would gain newfound relevance as secondary digital music market transactions would then involve “lawfully obtained” files.

Of course, one potential response—albeit somewhat cliché—to this suggestion could be, “easier said than done.” And perhaps such a response is merited, however, such a temporary reproduction exception in the Act could be fashioned appropriately. When addressing the issue of a temporary reproduction exception (of the same type created following *MAI Systems Corp.*), the “proper analytical approach . . . is to carve out a specific, narrowly-tailored exception.”¹⁷⁵ Thus, in light of the *ReDigi* case, the creation of a temporary reproduction exception that permits secondary digital music market transactions should apply strictly to digital transmissions operating within such a market. In addition to this limited

drive because the transfer from hard drive back to “cloud” storage—where content is sold—would trigger the “reproduction hurdle” and constitute infringement).

174. See generally *DMCA Section 104 Report*, *supra* note 99 (stating an in depth study and recommendation conducted by the U.S. Copyright Office regarding a potential “digital” first sale defense); S. 1621, 108th Cong. § 2(8) (2003) (bill proposing to amend the first sale doctrine to include a “digital” first sale exception); H.R. 1066, 108th Cong. § 4 (2003) (proposing to amend the first sale doctrine to include a “digital” first sale exception).

175. Eric H. Smith, *The Reproduction Right and Temporary Copies*, SOFTIC, at 7, http://www.softic.or.jp/symposium/open_materials/10th/en/smith-en.pdf (paper presented to Softic Symposium, Nov. 20–21, 2001) (last visited Mar. 10, 2014).

application, Congress should impose a number of mandatory requirements on companies such as ReDigi in order for this “temporary reproduction exception” to apply.

First, in order to fall under a temporary reproduction exception for a secondary digital music market, a digital music resale company (a “DMRC”) should be required to employ sufficient technological safeguards. The ReDigi “Verification Engine” and “Atomic Transmission” technology are actually a proper starting point, as—despite the ultimate finding of infringement—the court’s opinion focused on the infringing act of “temporary copying” rather than alleging that the protective technology was flawed.¹⁷⁶ While criticism exists as to the certainty that “transfer and delete” or “bit-by-bit” technologies will leave only one copy following a transfer, these technologies would ultimately be considered the first line of defense against infringing content. A DMRC, as a service provider where much of the site’s content is user-driven (given that users upload their legally purchased files to resell), will also have to comply with takedown requirements implemented in the Digital Millennium Copyright Act.¹⁷⁷ Ultimately, the first requirement that a DMRC would need to satisfy before a temporary reproduction exception should apply is the existence of secure and protective transaction technology that simulates a *de facto* physical transaction by leaving only *one* audio file following the sale.

Additionally, Congress should limit the number of times that a “used” audio file may be resold. Existing technology can track whether an audio file has been purchased from iTunes, Amazon, or other digital distributors. A limitation on the number of sales of a “used” digital file (essentially no different than a “new” digital file)¹⁷⁸ considers the vulnerability of new digital files in circulation and alleviates digital resale opponents’ concerns with the lack of degradability of used digital files by creating “digital wear and tear.” With this type of limitation on a secondary digital music market, the law could seek to achieve an efficient balance between secondary and primary digital music market transactions. Thus, if a DMRC detects that a digital music file has been sold the maximum number of times, that file is functionally removed from the market, forcing interested consumers to either purchase a new digital file or seek out a similar “used” digital file in a now shrunken market.

Finally, and arguably most crucial economically, a third requirement Congress should include for a DMRC to be eligible for a temporary

176. See generally *Capitol Records, LLC v. ReDigi Inc.*, 934 F. Supp. 2d 640, 640 (S.D.N.Y. 2013).

177. 17 U.S.C. § 512 (2014).

178. See *Is ReDigi Legal? Yes!*, *supra* note 9, at 649.

reproduction exception is a mandatory royalty system for the secondary market transactions. If a temporary reproduction exception were created without an explicit royalty requirement, DMRCs would not be obligated under the first sale doctrine—as it currently stands—to pay royalties to a copyright holder.¹⁷⁹ As one advocate argues, resale royalties “may hold the key to restoring the balance necessary for successful and fair operation of secondary markets in a digital world.”¹⁸⁰ One performance rights organization—SoundExchange¹⁸¹—provides “a model by which a digital resale royalty can be effectuated.”¹⁸² Imposing a requirement that DMRCs distribute adequate resale royalties to copyright holders—similar to ReDigi—contributes to the balance between consumer and copyright holder interests by making digital music more attainable to consumers while appropriately compensating copyright holders.

Mandatory resale royalties, along with sufficient technological safeguards and limitations on the amount of permissible resales, will enable an efficient secondary digital music market in which consumers’ freedom to exercise limited digital first sale rights also benefits copyright holders.

V. Conclusion

In a notable Supreme Court copyright case, Justice Potter Stewart famously declared, “when technological change has rendered its literal terms ambiguous, the Copyright Act must be construed in light of this basic purpose.”¹⁸³ Granted that Judge Sullivan’s opinion in *ReDigi* states that the text of the statute is unambiguous and can be sufficiently applied to the facts of the case, there is nonetheless a strong indication that the text is outdated. In this particular case, operating under “outdated” statutory text can be just as detrimental as operating under an “ambiguous” one.

It seems unlikely that Congress was able to meaningfully contemplate the effects of today’s digital media markets when it enacted the Act—as evidenced by the inclusion of “any method now known or later developed”¹⁸⁴ in the statute. Today’s Congress, however, has the ability to appreciate the digital media advancements in the music context, and therefore can accommodate a secondary digital music market by intelligently amending current copyright law. Learning from the clash

179. 17 U.S.C. § 109.

180. Serra, *supra* note 24, at 1787.

181. *About, SOUNDEXCHANGE*, <http://www.soundexchange.com/about/> (describing SoundExchange as an “independent nonprofit performance rights organization that collects and distributes digital performance royalties to featured artists and copyright holders”) (last visited Mar. 10, 2014).

182. Serra, *supra* note 24, at 1797–98.

183. *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 155 (1975).

184. 17 U.S.C. § 101.

between existing copyright law and innovative ReDigi technology, Congress should create a “temporary reproduction” exception in copyright law for qualifying DMRCs. The secondary digital music market will of course need additional regulation, requiring that DMRCs: (1) operate with proper “de facto” transfer technologies, (2) prohibit sales of digital files that fall within a determined resale limitation, and (3) implement a mandatory resale royalty system. The resulting system would enable a secondary digital music marketplace to operate in a manner that balances the interest of consumers and copyright holders by giving consumers more autonomy with their digital music collection while maintaining compensation for the artists and copyright holders that create such collections.

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